WINSTON
& STRAWN
LLP

North America Europe Asia

35 W. Wacker Drive
Chicago, IL 60601
T +1 312 558 5600
F +1 312 558 5700

September 16, 2016

By E-mail: regs.comments@federalreserve.gov

Robert de V. Frierson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Re: Capital Requirements for Supervised Institutions Significantly Engaged in Insurance Activities (Docket No. R-1539; RIN 7100 AE 53)

Dear Sir:

We are writing to comment on the Federal Reserve Board's (the "FRB") advance notice of proposed rulemaking ("ANPR")[1] regarding approaches to regulatory capital requirements for depository institution holding companies significantly engaged in insurance activities.[2] Winston & Strawn LLP ("Winston") represents a group of affected insurance companies that own thrifts as insurance depository institution holding companies ("IDIHCs"). In addition, to facilitate our understanding of the twelve discrete institutions affected by the ANPR, Winston formed the "Thrift Discussion Group" (the "Group") made up of nearly all twelve institutions, and solicited feedback from the Group on the issues outlined in the ANPR. Those companies included in the Group, of course, would be directly affected by capital requirements imposed by the FRB on IDIHCs, and this letter expresses the support, considerations and concerns of the Group regarding the ANPR.

The Group fundamentally and strongly agrees that capital is an important safeguard to protect the safety and soundness of financial institutions. We appreciate the FRB's efforts reflected within the ANPR to address differences between banking and insurance entities, including differences in business models, organizational structures, accounting practices, and functional regulation. At the same time, we recognize the complexity of these issues and express below some concerns regarding proposed capital regulation approaches, and highlight areas we believe need additional clarification.

*I. Group Member Comparison*

At the outset, we consider it important to provide some background information on the twelve institutions that would be impacted by any holding company capital requirements imposed by the FRB.

[1] 81 F.R. 38631 (June 14, 2016).
[2] We represent the views of the Group and no member of the Group is a Systemically Important Financial Institution ("SIFI"). We therefore do not separately represent the views of any SIFI and have limited our comments on the ANPR in each instance to its possible effect on IDIHCs. We make no comment on the ANPR as it may be applied to SIFIs.

To that end, we surveyed the Group for information that provides some context to the disparity in size, geographic footprint, corporate organization and other aspects of their businesses. The diversity of institutions includes: (i) their headquarters are located throughout the United States from the West Coast, to the Midwest, to the deep South, and the Northeast—which correspondingly impacts the primary state insurance regulator, Reserve Bank, OCC, or FDIC office serving as the primary regulator; (ii) operations for these institutions include those heavily concentrated in a single state, others are focused regionally (such as operations throughout a dozen Midwestern states) and others are leading insurers on a national or international scale; (iii) corporate structures are quite varied, including mutual organizations, membership organizations, reciprocal inter-insurance exchanges, and fraternal benefit societies; (iv) institutional size of these organizations ranges from annual revenues of approximately $5 billion to more than $100 billion; (v) the number of employees per institution ranges from less than 1,000 employees to in excess of 50,000 employees; (vi) the number of business and retail customers served by institutions varies widely—with business customers at smaller institutions numbering less than 500, larger institutions serving more than 50,000 businesses and retail customers served by institutions ranging from less than 10,000 customers to more than 50 million customers; and (vii) finally, many of these institutions have community- and public-oriented mission statements, such as serving military members and their families, farmer cooperatives, or helping drivers needing assistance with auto clubs.

Despite the above diversities, two common elements shared by a large number of the impacted companies are that (i) the ultimate parent company is usually organized as an operating insurance company and (ii) the companies generally have been in business since before the Great Depression. We highlight these two common elements because (1) the regulation of insurance companies is a new area of supervision for the FRB, particularly with reference to capital standards, and (2) these companies have withstood significant financial turmoil in the past—over at least 14 recessions, with whipsawing inflation rates, and in some cases stagflation—in each instance, the potentially impacted companies have come out the other side of the storm, and have done so without FRB oversight or FRB capital standards. Recognizing that these twelve institutions are few in number, yet are a significant and diverse segment of the insurance industry, it is incumbent on the FRB to carefully consider the way in which to proceed when imposing group-wide capital assessments on these insurance companies.

Additionally, it is worth noting that many insurance companies, including members of the Group, use Statutory Accounting Principles ("SAP") rather than Generally Accepted Accounting Principles ("GAAP"). The use of SAP standards is generally considered more conservative than GAAP. Additionally, and as discussed *infra*, Congress has specifically rejected the FRB's authority to impose GAAP accounting on SAP filers.[3] The Group is concerned that elements of the ANPR may suggest the imposition of GAAP requirements in certain circumstances.

[3] 12 U.S.C. § 5371(c)(3)(A).

*II. Preferred Alternative—Continued State Regulation*[4]

The ANPR solicits comments relating to preferable alternative approaches to those described in the release. The Group suggests a reasonable alternative that the FRB should reconsider is not to apply capital requirements to insurance companies, but rather to defer to existing state insurance regulatory capital requirements for insurance companies. Clearly, the FRB has the legal authority to defer to the state insurance regulators. Indeed, the FRB should do so since state insurance regulators have time-tested experience and expertise in determining what constitutes adequate insurance company capital. In conformance with the FRB's own policy, as well as that articulated in Dodd-Frank, the FRB should defer to the industry's principal regulators. Out of comity for other regulators and to avoid unnecessary expense and complication, the FRB should not impose capital requirements on any parent insurance company if the company's State regulator believes that the company's capital is adequate. If the FRB reasonably finds that a particular State regulator's capital requirements are insufficient, it may reserve the right to make, by order, a reasoned finding to that effect and then impose its own capital requirements. However, in the absence of such a finding, the FRB should respect and defer to state insurance regulators. Congress, in enacting source of strength statutes and provisions that are specific to IDIHCs, has made an election to defer to the state insurance regulators and the FRB should be guided by the deference in any rulemaking or interpretive process relating to insurance companies.

*III. Support for the BBA*[5]

Despite our belief that the FRB should defer to state regulators, the FRB has the legal authority to impose a capital framework on IDIHCs and the Group acknowledges the considerable and careful thought the FRB has put into how to do so.

The Group appreciates the FRB's willingness to consider the Building Block Approach ("BBA") discussed in the ANPR and to apply that approach to IDIHCs. The Group supports the general BBA framework outlined by the ANPR—which will (1) subject an insured depository institution to capital standards set by its primary federal regulator, (2) require companies primarily engaged in insurance to meet standards set by relevant state insurance regulatory authorities, and (3) aggregate the required capital across the entire enterprise in order to determine an overall capital requirement. The Group, in particular, considers the essential element to be that the BBA will respect the existing insurance regulatory framework by using the standards set at the state level as the basis for forming the individual components that will then be used to establish the enterprise's overall capital. As mentioned previously, this existing regulatory capital framework has served the public very well through many economic cycles.

The Group notes the following beneficial aspects of a BBA that has been properly vetted by the industry and modified for any outstanding issues and uncertainties: (1) the BBA utilizes existing capital frameworks that were specifically designed for insurance companies, taking into account their unique risk

[4] This addresses Question 1 in the ANPR.
[5] This addresses Questions 6 and 12 in the ANPR.

characteristics, and therefore, the BBA could be implemented reasonably quickly and more efficiently than a newly created capital standard;[6] (2) the BBA would help normalize the operations of domestic and international insurers, allowing easier comparison of the financial health of institutions across the industry and across jurisdictions; (3) the BBA will provide for differentiated treatment of the risks inherent in the various lines of business and would therefore appropriately reflect differences between insurers, banks and unregulated affiliates; and (4) the BBA does not require the use of a consolidated balance sheet, thereby enabling the FRB to permit multiple accounting regimes, which again may allow it to be implemented earlier and with less disruption to the affected institutions.

Because we believe that the BBA builds on the existing state-based regulatory framework and has the additional benefits described above, the Group therefore favors the BBA over the Consolidated Approach described in the ANPR.

*IV. Details Needed on BBA*[7]

The Group understands, at this early stage in the rulemaking process, the FRB has not decided upon many details that would be crucial as to how the BBA would actually work in practice. Those details, however, are crucial to the way in which any regulations in this area should proceed.

a. Capital—Surplus Notes[8]

Important details include how "capital" would be defined and what would qualify as "capital." The ANPR discusses utilizing a uniform definition of available capital on a fully consolidated basis. In considering this issue, the Group has a strong preference that capital components utilized by the FRB should match capital components permitted under State insurance laws. For example, surplus notes are included within the definition of capital under current insurance capital requirements promulgated by state insurance regulators. Despite the Group's understanding that the FRB prefers equity capital, the Group suggests the FRB give serious consideration to deeming surplus notes to satisfy capital requirements under the BBA. Such notes are deeply subordinated to policyholder and all other creditor claims and are reported as policyholders' surplus despite their debt-like features. Interest payments and principal repayments cannot be made on surplus notes without prior insurance regulatory approval. Surplus notes have been part of insurance company capital and surplus since the 1960s. State insurance laws mandate that such notes be treated as policyholders' surplus and not debt. As discussed above, Congress' second goal in the Insurance Capital Standards Clarification Act of 2014 (the "Collins Fix")[9] was to ensure that an IDIHC that files financial statements in accordance with SAP shall not be required by the FRB to prepare financial statements in accordance with GAAP; therefore, Congress has made an

[6] As a single exception to this, we note that title insurers are not subject to existing risk-based capital regimes under state insurance statutes, and there does not appear to be a readily available "building block" capital requirement for title insurers. We understand that First American Financial, the only IDIHC primarily engaged in the business of title insurance, is submitting a separate letter regarding this issue.
[7] This addresses Question 7 in the ANPR.
[8] This addresses Question 21 in the ANPR.
[9] Codified at 12 U.S.C. § 5371(c)(1).

express decision not to disrupt the accounting practices of the insurance industry. In that regard, the Group suggests that the FRB should respect Congress' intent, as well as historically conservative accounting practices, and provide for similar capital treatment of surplus notes.

b. Calculation of Ratios

Another important detail is reaching an understanding on the method to compute capital ratios. As with the Group's overall strategic approach to the ANPR issues, we urge the FRB, consistent with the BBA's proposed benefit of ease of administration, to use existing standards promulgated by state insurance regulators to compute capital ratios and to defer to such processes and determinations.

c. Definition of "Subsidiary"

Another important issue is whether the BBA would apply to each subsidiary as if it were a stand-alone entity. We presume that the definition of the term "subsidiary" would be the same as that used in the Home Owners Loan Act ("HOLA")[10] and thereby incorporate the Bank Holding Company Act ("BHCA")[11] definition of "control" as ownership of 25 percent or more of a class of voting securities.

d. Records and Reports

In keeping with the advantages of the BBA's goal of timely and efficient implementation, we suggest that the FRB consider records and reports currently prepared for state insurance purposes sufficient for institutions to comply with any new capital regulations. The Group also requests the FRB utilize timing of reports consistent with the timing currently used by State insurance regulators. For example, state-specific Risk Based Capital ("RBC") reporting frequency is annual based on the institution's fiscal year-end numbers.[12] A more frequent calculation of RBC would be, of necessity, premised on assumptions and estimates that are not otherwise calculated in the insurance business. This is generally due to the fact that the risks in the insurance businesses do not dramatically change quarter to quarter and consequently a more rigorous annual review process has been shown to have more evenly predictive qualities than quarterly calculations. In addition, more frequent reporting leads to a heightened burden of preparing reports without offsetting benefits. The Group notes as well that the FRB conducts continuous supervision of its institutions and, therefore, would be alerted to any out-of-the-ordinary changes to the institutions' risk profiles.

e. Aggregation of Capital

State insurance regulators have long regulated the levels of capital required of insurance companies and their affiliates. For the most part, state insurance regulators have done an excellent job. Additionally, coordinated efforts of state insurance regulators are conducted through the National

[10] 12 U.S.C. § 1461-1470.
[11] 12 U.S.C. § 1841-1852.
[12] Again, we note the lack of a risk-based capital approach for title insurers, and the absence of any other readily available alternative, and refer the FRB to First American Financial's separate letter on its unique circumstances.

Association of Insurance Commissioners ("NAIC"). The NAIC is a policy, standard-setting and regulatory support organization composed of the chief insurance regulators from all 50 states, the District of Columbia and five U.S. territories and works collectively with input from industry and experts to establish standards and best practices, conduct peer reviews, and coordinate information on regulatory oversight. Thus, the Group appreciates that the BBA implicitly recognizes this source of expertise by largely relying on such requirements. The BBA would require aggregate capital that is the sum of capital requirements at each subsidiary. Fundamentally, members of the Group take the position that insurance business legal entity capital is not fungible, particularly between an institution's subsidiaries. The BBA appears in its proposed form to respect that principle and, thus the Group prefers that approach to the enterprise-wide approach described in the ANPR's Consolidated Approach.

The Group also would observe that an aggregated IDIHC capital number may not be meaningful because, in the insurance industry, capital of different affiliates is not pooled, but rather is required to be retained to specifically cover the risks to the insureds of the individual legal entity. Insurance companies do not generally transfer capital from one insurance legal entity or affiliate to another. Instead, separate affiliates may sometimes be established to protect the enterprise from risks assumed by one entity from impacting other affiliated entities. Thus, while the aggregate capital that an IDIHC and its subsidiaries hold may be a rough gauge of financial strength, it may not be indicative of what capital is available to absorb loss at a given affiliate.

f. Unregulated Entities[13]

In the case of regulated subsidiaries, capital requirements would be determined by the rules of the appropriate supervisor. However for those entities that are neither banking nor insurance companies (the ANPR calls these "unregulated entities"), the FRB proposes to apply Regulation Q, and thus would default to bank-like risk-weighted capital requirements. The Group believes this standard should be reconsidered as inappropriate in this context, and is concerned about the imposition of such capital requirements.

The Group generally questions the practical applicability of using Regulation Q to risk-weight the assets in these subsidiaries. The concern stems from the nature of the risk-weighting methodology of Regulation Q. Regulation Q risk-weighting is generally a measure of credit risk. So, for example, if the subsidiary assets are commercial in nature, most commercial assets do not present credit risk, as we discuss at greater length below. It is not readily apparent, *e.g.*, how inventories of finished goods, work in progress, raw materials, longer-term assets such as property, plant, or equipment or, in the case of an unregulated title insurance company affiliate, title plants and records, could be rationally risk-weighted under Regulation Q. It is not even apparent how the holding of such assets creates credit risk for the enterprise, let alone indirectly to a bank affiliate. If the FRB has in mind a method of weighing such risks, we suspect that it would be quite complex and interfere with some of the key strengths of the BBA, *i.e.*, efficient use of existing frameworks, expeditious implementation, and low burden. One alternative to the approach advocated by the FRB would be to exempt companies that do not engage in "financial

[13] This addresses Question 14 in the ANPR.

activities," as such term is defined in 12 U.S.C. § 1467b following the passage of the Dodd-Frank Act. We believe that such an exclusion is consistent with the intent of Congress to not subject traditional operating companies to FRB supervision and bank-like capital standards.

Other key issues, such as the treatment of goodwill and intangible assets, present additional difficulties in terms of proper accounting treatment as such items are historically treated differently with respect to a commercial entity as opposed to a bank or insurance entity. The Group believes that the FRB should engage the impacted institutions in additional dialogue with respect to these issues to understand the current activities and the unintended consequences that may result from changes required.

Further, in the particular context of the BBA's aggregation of capital requirements of commercial firms, the FRB needs to take into account the fact that many insurance company subsidiaries hold investments in real estate and other assets through special purpose wholly-owned or majority-owned limited liability companies or limited partnerships. Such LLCs and LPs are not regulated on any ongoing basis and, thus, under the BBA, would give rise to capital requirements based on Regulation Q, even though the assets are essentially insurance company assets that should be subject to state insurance regulation capital requirements, not bank-like capital requirements. Such investments support insurance operations to the same extent as if the investments had been directly held by the parent insurance company. These investments in special-purpose LLCs and LPs that only hold real estate and other assets are usually treated as investments under the equity method of accounting. The Group believes these special purpose vehicles, held by insurance companies to support insurance operations, should continue to be included in insurance risk-based capital calculations and not subjected to separate, special FRB capital treatment.

Finally, another alterative that the Group recommends is to provide for exemptions or a materiality test whereby the FRB would take a more nuanced approach to unregulated affiliates. This would streamline implementation of the BBA as it could (1) permit the institutions to disregard for purposes of capital calculation any entities that the FRB properly determines should be excluded and/or (2) permit simplified capital treatment of entities that the FRB determines must be included, but are not considered material.

g. Determining Significant Engagement in Insurance Activities[14]

Key to determining the applicability of the BBA is how the FRB will determine that an SLHC is an IDIHC. Indeed, the FRB seeks comment on the criteria that should be used to determine which supervised institutions should be subject to regulatory capital requirements tailored to the business of insurance. The ANPR suggests that a supervised insurance company could become subject to tailored capital rules based on the significance of the insurance activities for the consolidated firm, specifically positing that the test might be 25 percent or more of total consolidated assets in insurance underwriting (other than underwriting credit insurance risk). We believe that this issue requires further study, and that possible alternatives include considering an institution to be substantially engaged in insurance if: (1) the

[14] This addresses Question 3 in the ANPR.

top-tier holding company is an insurance underwriting company; or (2) if the top-tier holding company is not an operating insurance company, the top-tier holding company holds 25 percent or more of its total consolidated assets in insurance underwriting companies (whether held through subsidiaries, directly, or some combination thereof).

h. Adjustments and Scalars[15]

We understand that the FRB may consider the use of adjustments and scalars in the context of international insurance regulatory schemes. However, the Group is concerned that the FRB's reservation of authority to adjust and scale is not described as being limited to that authority and, thus, we are concerned that these tools may be applied domestically to various State capital requirements for accounting differences and for perceived stringency of regulation.[16] The ability to adjust and scale domestic state insurance capital requirements eliminates key strengths of the BBA. Adjusting and scaling state insurance regulatory capital requirements appears to be subject to arbitrary judgment, is not consistent with efficient use of existing frameworks and is not likely to be expeditiously developed. Regulatory costs would be high considering 50 State capital regimes and the stringency of regulation by each of the 50 States, comparing each state's capital regime, ranking them, and even trying to quantify differences.

In order for a state to be accredited by the NAIC, a state must submit a self-evaluation guide, undergo on-site examinations by a team of insurance experts, submit to annual reviews and correct any identified weaknesses or areas where the state is out of conformance with accreditation standards. Among the accreditation standards are the state's conformance to recommended risk-based capital standards and SAP. Through the accreditation process, the states are able to achieve an incredible level of consistency and, therefore, there should be no need for the FRB to impose interstate adjustments or scalars. Based on the ongoing and intensive requirements, the Group feels that if a state insurance regulator has met the standards of the independent NAIC, the FRB should be satisfied with that accreditation and the NAIC's judgment of the state insurance regulator's effectiveness and stringency of that regulator's oversight of insurance companies. No compelling reason has been proffered as to why the FRB should substitute its judgment for that of the NAIC. We are not aware of any criticism of the NAIC which alleges it has not done an excellent job or is likely to be less effective in the future. In the absence of such criticism, we believe that the FRB should defer to the NAIC on the stringency of a particular state's regulation of insurance companies.

Additionally, and from a practical perspective, insurance risk-based capital is largely the same state to state. After careful study and considerable deliberations, the NAIC adopted model risk-based capital requirements that, in turn, have been adopted in every state. Those requirements and their risk-

[15] This addresses Questions 8, 15, and 19 in the ANPR.

[16] This concern is limited to domestic insurance companies; we offer no opinion on adjusting and scaling for foreign insurance accounting or foreign regulator stringency. Similarly, we acknowledge that a case could be made that adjustment and scaling may be appropriate between, for example, property and casualty ("P&C") insurance, on the one hand, and life insurance, on the other. Our comments are limited to the proposition that adjustment and scaling should be done among State P&C insurance regulators or among State life insurance regulators.

weightings are periodically reviewed by state insurance commissioners who serve on a sub-group of the NAIC devoted to expertly and carefully risk-weighting different assets and are available for consultation in the event of an unusual financial instrument. The work of the NAIC staff reduces the chance of disparities in capital treatment from state to state. Additionally, while some members of the Group, or certain Group member subsidiary companies, may not file risk-based capital reports, the NAIC is actively engaged with industry members in formulating an alternative approach for such institutions.

For the FRB to assess the stringency of a state's insurance regulation, when the NAIC already does so, would unnecessarily complicate the setting of IDIHC capital requirements. The Group would urge the FRB to make clear that scalars are intended for use solely in the context of international insurance regulatory regimes.

*V. APA Requirement to Consider the Benefit Versus the Cost of Proposed Regulation.*

Under the Administrative Procedures Act (the "APA"), any proposal of this magnitude requires the FRB to balance the costs of the proposed regulation against the benefits of any eventual proposal. In addition, the FRB needs to tailor any eventual proposal to identify where there may be an actual problem to be addressed, and if so, narrowly define the solution. In particular, when dealing with adequate capital in the insurance industry, the FRB should consider the most appropriate and least costly alternative solution. The Group believes that solution quite clearly suggests that any rule resulting from this ANPR should derive from the premise of deferring to expert state insurance regulators. By law, the FRB is obligated, in determining the administrative compliance requirements of new regulations that impose requirements on insured depository institutions, to consider any administrative burdens that such regulations would place on such institutions. Further, two Presidential Executive Orders have urged that regulatory agencies propose and adopt regulations only upon reasoned determinations that their benefits justify their costs. Any proposed regulation that stems from this ANPR should consider whether any incremental benefit beyond what capital is already required of insurance companies under state law justifies the costs.

*VI. The FRB Should Reconsider Whether Such Capital Regulation is Appropriate.*[17]

We believe it is important to observe, in particular, that the fundamental premise supporting the ANPR states:

> "the [FRB] **must** establish minimum leverage capital requirements and minimum risk-based capital requirements that apply (a) on a consolidated basis and (b) are at least as stringent as the generally applicable capital requirements that applied to insured depository institutions ("IDIs") at the time the Dodd-Frank Act was adopted, as well as current generally applicable IDI capital requirements. The Dodd-Frank Act has been

[17] This addresses Question 1 in the ANPR.

> amended to allow the [FRB] to tailor those minimum capital requirements as they would apply to persons regulated by state or foreign insurance regulators"[18] (emphasis added).

The FRB's assessment that it is required to implement such standards may conflict with both Congressional intent and the statutory language of the Dodd-Frank Act amendment cited in the ANPR (the Collins Fix). Indeed, one of the two primary purposes[19] of the Collins Fix was to clarify that the FRB **is not required** to establish minimum leverage or minimum capital standards for insurers.[20] Prior to the Collins Fix, the FRB had taken the position that it had no discretion but to apply bank-like capital requirements to IDIHCs.[21] Fearing that the FRB might choose to apply such bank-like capital requirements to IDIHCs, the insurance industry and Congress worked together in an expedited fashion to draft and approve the Collins Fix. The overwhelming, bipartisan support and sheer speed with which the Collins Fix moved from introduction in the Senate, to passage by both houses, Presidential signature and effective date should serve as a strong indicator to the FRB of how clearly Congress believed that IDIHCs should not necessarily be subject to FRB capital standards.[22] Thus, while the FRB may have retained the authority to implement capital standards for these covered institutions, the FRB **is not required** to impose capital requirements. The express implication of the Collins Fix was Congressional approval of, and provision of the legal authority for, the FRB to altogether decline to impose capital requirements on insurance companies and instead defer to the expertise of state insurance regulators where the task of regulating insurance company capital historically has been conducted.

In the context of the ANPR, we would also observe that the FRB rejected an entirely acceptable alternative, perhaps based on a mistaken understanding of its statutory mandate.[23] The ANPR stated:

> "The [FRB] also reviewed an approach that entirely excluded insurance subsidiaries and applied capital requirements only to the non-insurance parts of the supervised firm. *This approach would, by definition, not capture all the material risks of the organization.*

[18] 81 F.R. 38632 (June 14, 2016).
[19] The second purpose expressly provides that an IDIHC that files financial statements with a state insurance regulator or the NAIC utilizing only SAP in accordance with State law should not be required by the FRB to prepare such financial statements in accordance with GAAP. 12 U.S.C. § 5371(c)(3)(A).
[20] See 12 U.S.C. § 5371(c)(1) "[i]n establishing the minimum leverage capital requirements and minimum risk-based capital requirements ..., the appropriate Federal banking agencies *shall not be required* to include for any purpose of this section (including in any determination of consolidation), a person regulated by a state insurance regulator ... to the extent that such person acts in its capacity as a regulated insurance entity" (emphasis added).
[21] *See, e.g.*, 78 F.R. 62018 Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Capital Adequacy, Transition Provisions, Prompt Corrective Action, Standardized Approach for Risk-weighted Assets, Market Discipline and Disclosure Requirements, Advanced Approaches Risk-Based Capital Rule, and Market Risk Capital Rule (which noted the FRB's intention to apply bank-like capital standards, but "[a]fter considering the comments received from SLHCs substantially engaged in commercial activities or insurance underwriting activities, the FRB has decided to consider further the development of appropriate capital requirements for these companies, taking into consideration information provided by commenters as well as information gained through the supervisory process.").
[22] S. 2270 had 33 co-sponsors (equally divided between Democrats and Republicans), passed the Senate with an amendment by unanimous consent on June 3, 2014, and was considered by unanimous consent and passed without objection by the House on December 10, 2014.
[23] This addresses Question 38 in the ANPR.

> While section 171 of the Dodd-Frank Act, as amended, permits the [FRB] to exclude state and foreign regulated insurance entities in establishing minimum consolidated leverage and risk-based capital requirements, *the parent holding company should be a source of capital strength to the entire entity, including to the subsidiary insurance companies* and IDIs. To do this effectively, *a consolidated capital requirement must take into account the risks within the consolidated organization, including insurance risks.*"[24] (emphases added).

Respectfully, that conclusion by the FRB in the ANPR is contradictory to the specific statutory language and the intent of Congress. The statutory source of strength requirement pertains to the holding company serving as a source of strength to the depository institution only, and not to the entire insurance company.[25] The statute provides "[t]he appropriate Federal banking agency for a bank holding company or savings and loan holding company shall require the bank holding company or savings and loan holding company to serve as a source of financial strength for any subsidiary of the bank holding company or savings and loan holding company **that is a depository institution**"[26] (emphasis added). Thus, the FRB's premise that an IDIHC should be a source of strength to its insurance subsidiaries is without legal basis, and we believe, therefore, that the FRB should reconsider its analysis and conclusion relating to this proposed alternative. That is, the FRB should reconsider the alternative of excluding insurance subsidiaries from any capital requirements it would consider proposing for IDIHCs. In addition, in the next steps following the ANPR, the FRB should avoid using this expanded view of the source of strength to justify additional regulatory requirements. Such requirements should proceed from the carefully tailored statutory authority.

Further, the source of strength requirement is different for IDIHCs that are SLHCs as opposed to traditional bank holding companies.[27] Section 1844(g) provides that, if the FRB requires an SLHC that is an insurance company (or an affiliate thereof that is an insurance company) to provide funds to a subsidiary bank, the FRB shall promptly notify the State insurance authority for the insurance company.[28] Section 1844(g) further provides that any action of the FRB that requires an SLHC to provide funds to a subsidiary bank shall not be effective nor enforceable if (A) such funds are to be provided by an SLHC that is an insurance company (or affiliate insurance company thereof) and (B) the State insurance authority for the insurance company determines in writing sent to the SLHC and the FRB that the SLHC shall not provide such funds because such action would have a material adverse effect on the financial condition of the insurance company.[29] Thus, by federal law, in the case of IDIHCs where the top-tier entity is an operating insurance company, the requirement that such IDIHCs be sources of strength to their IDIs is balanced with their duty to maintain their own strong financial conditions. The significance

[24] 81 F.R. 38637 (June 14, 2016).
[25] 12 U.S.C. § 1831o-1(a).
[26] *Id.*
[27] *See* 12 U.S.C. § 1831o-1(c)(1), which provides that the provisions of 12 U.S.C. § 1844(g) shall apply to an SLHC that is an insurance company (and any affiliate that is an insurance company).
[28] 12 U.S.C. § 1844(g)(2).
[29] 12 U.S.C. § 1844(g)(1).

of this appears to be that the FRB's fundamental premises—that the FRB is required to impose capital requirements on IDIHCs, and require such companies to be a source of strength to their insurance subsidiaries as well as a source of strength without limit to their IDI(s) may not only be misplaced, but in fact is subject to being overruled by the relevant State insurance authority.

We appreciate the opportunity the FRB has given us to express, on behalf of the Group, views on this very important public policy issue. We would be happy to respond to any questions relating to this comment letter or the views expressed within it.

Respectfully submitted:

Christine Edwards
*Chair, Bank Regulatory Practice*
(312) 558-5571
cedwards@winston.com

Julius L. Loeser
(312) 558-5985
jloeser@winston.com

Sterling Sears
(312) 558-6208
ssears@winston.com